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No. 84-1772

IN THE
SUPREME COURT OF THE UNITED STATES

October Term 1985

HARRY H. and ALICE G. KARMUN,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONERS' REPLY BRIEF

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August 2, 1985

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I. THE RECENT DECISIONS OF THIS COURT IN MONTANA v. BLACKFEET TRIBE OF INDIANS AND COUNTY OF ONEIDA v. ONEIDA INDIAN NATION REAFFIRM THE IMPORTANCE OF GRANTING REVIEW OF THE NINTH CIRCUIT'S DECISION IN THE INSTANT CASE.

The instant case represents a classic conflict between two bodies of law, in this instance federal Indian law and federal income tax law. Traditional notions of tax law require that exemptions from taxation cannot be granted by implication but must be clearly expressed. In contrast, a well established principle of Indian law is that statutes affecting Indians are to be liberally construed to the benefit of the Indian. Petitioners submit that under the circumstances raised by the present case this Court must follow the holding in the seminal federal Indian taxation case of Squire v. Capoeman, 351 U.S. 1 (1956) and reconcile the conflict by granting them an exemption from federal income tax.

Succinctly stated, the Court in Squire held that income directly derived from an Indian's own trust property is exempt from federal taxation during the period of the trust. Because of the nature of the property and related income in this case -- namely income directly derived from reindeer held in trust under express provisions of the Reindeer Industry Act of 1937, 25 U.S.C. §§ 500 et seq. -- Squire is the only decision of this Court directly on point and must therefore control the result. Other decisions cited by Respondent involve extensions beyond the Squire rule and are thus distinguishable.[1/]

[1/] See discussion in Section II, infra. Note also that the cases cited by Respondent in the latter half of n. 4 (Br. in Op. p. 4) are examples of extensions beyond the basic Squire rule: either someone other than the primary trust beneficiary sought the tax exemption or the income was not directly derived from the beneficiary's trust property.

Two recent decisions from this Court's last term provide additional strength to the Squire Court's reconciliation of conflicting principles of federal Indian and tax law in favor of the Indian in "directly derived" income cases. First is the decision in County of Oneida v. Oneida Indian Nation, ___ U.S. ___, 105 S. Ct. 1245 (1985), where this Court announced that the "canons of construction applicable in Indian law are rooted in the unique trust relationship between the United States and the Indians." 105 S. Ct. at 1258. Second is the case of Montana v. Blackfeet Tribe of Indians, ___ U.S. ___, 105 S. Ct. 2399 (1985), where, after quoting the above passage from Oneida, this Court applied the canons of statutory construction to defeat the imposition of a state royalty tax to income earned under leases entered into pursuant to the

provisions of a 1938 federal law on the ground that the law did not expressly authorize the imposition of taxation.

> Indeed, the Court has held that although tax exemptions are to be construed narrowly, in "the Government's dealings with the Indians the rule is exactly the contrary. The construction, instead of being strict, is liberal. . . ." Choate v. Trapp, 224 U.S. at 675.

Montana v. Blackfeet Tribe of Indians, supra, 105 S. Ct. at 2404, n. 4.

Oneida and Blackfeet are important to the present case for several reasons. First, because the reindeer owned by Petitioners are the subject of an express federal trusteeship the canons of construction rooted in that unique trust relationship must be applied to reconcile the conflict between federal Indian and tax law. Oneida, supra. And second, because this is an Indian tax case, the Reindeer Industry Act must be liberally

construed to confer an exemption from federal taxation for income directly derived from the sale of reindeer and reindeer products. Blackfeet, supra. Thus, the analytical approach used by the Court in Squire to imply an exemption has been soundly reaffirmed by this Court in Oneida and Blackfeet, and should be the basis for conferring an exemption here.

II. RESPONDENT'S EFFORT TO NARROWLY INTERPRET SQUIRE MUST FAIL.

Respondent misreads the decision in Squire in two key respects. First, Respondent would have the Court believe that the Squire Court adopted the "settled principle" from Choteau v. Burnett, 283 U.S. 691, 696 (1931) that the "intent to exclude [from taxation] must be definitely expressed." (Br. in Op. p. 5.) Quite the contrary is in fact the case. The Court in Squire expressly distinguished Choteau on the ground that

the Indian in question there was competent and had unrestricted control over his land. Squire, supra, 351 U.S. at 9, n. 19. With respect to such a case the Squire Court clearly said that "in the ordinary affairs of life . . . [Indians] are subject to the payment of income taxes as are other citizens." Id. at 6.[2/]

[2/]Respondents' reliance on Mescalero Apache Tribe v. Jones, 411 U.S. 145 (1973); and Superintendent v. Commissioner, 295 U.S. 418 (1935) is also misplaced. (Br. in Op. at pp. 3 and 5.) Neither are "directly derived" trust income cases: the Squire Court distinguished Superintendent because the income there was "reinvestment" income. Squire, supra, 351 U.S. at 9. Mescalero is easily distinguishable: the Indian property there, though tribally owned, was outside the boundaries of the Mescalero Reservation and not held in federal trust or restricted status. Mescalero, supra, 411 U.S. at 145-6. Thus in the view of the Court in Squire these would be nothing more than ordinary tax cases.

The fundamental distinguishing factor which makes Squire so important is that in cases involving trust property and income derived directly therefrom the rules of the game are different: an affirmative showing must be made that Congress intended to tax the primary trust beneficiary. Id. at 8.

Second, Respondent attempts to limit the application of Squire on the basis that it applies only to income directly derived from allotted land. (Br. in Op. pp. 3-4.) Respondent, however, can cite to no case which establishes that principle nor can any argument be found in Respondent's brief in opposition distinguishing between the trust established pursuant to the General Allotment Act, 25 U.S.C. §§ 331 et seq., and that established by the Reindeer Industry Act. Again, as this Court in

Oneida and Blackfeet make clear: the canons of construction have their origin in the trust and those canons compel a different result in trust based Indian income tax cases from cases involving the taxation of ordinary citizens.

III. CONCLUSION

Alaskan reindeer may indeed be unique Indian trust property but that factor, standing alone, cannot legitimately be the basis for the Ninth Circuit's departure from the principles established in Squire in denying the Karmuns an exemption from federal income taxation. Trust reindeer have all the classic incidents of Indian trust property and, during the period of the trust, should be treated accordingly for tax purposes. The recent decisions of this Court in Blackfeet and Oneida only serve to confirm the need to correct the Ninth

Circuit's departure from Squire and apply the correct rules of construction to reconcile the conflict inherent in federal Indian and tax law cases in favor of the Indian when directly derived trust income is at issue.

Respectfully submitted,

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